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In the

Supreme Court of the United States

OCTOBER TERM, 1971

THOMAS RICCI,

Petitioner,

vs.

CHICAGO MERCANTILE EXCHANGE, an Illinois not-for-profit corporation, EVERETTE B. HARRIS, WILLIAM PHELAN, LEO MELAMED, THE SIEGEL TRADING COMPANY, a corporation, and JOSEPH E. SIEGEL,

Repondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

BRIEF FOR RESPONDENTS CHICAGO MERCANTILE EXCHANGE, EVERETTE B. HARRIS, WILLIAM PHELAN AND LEO MELAMED

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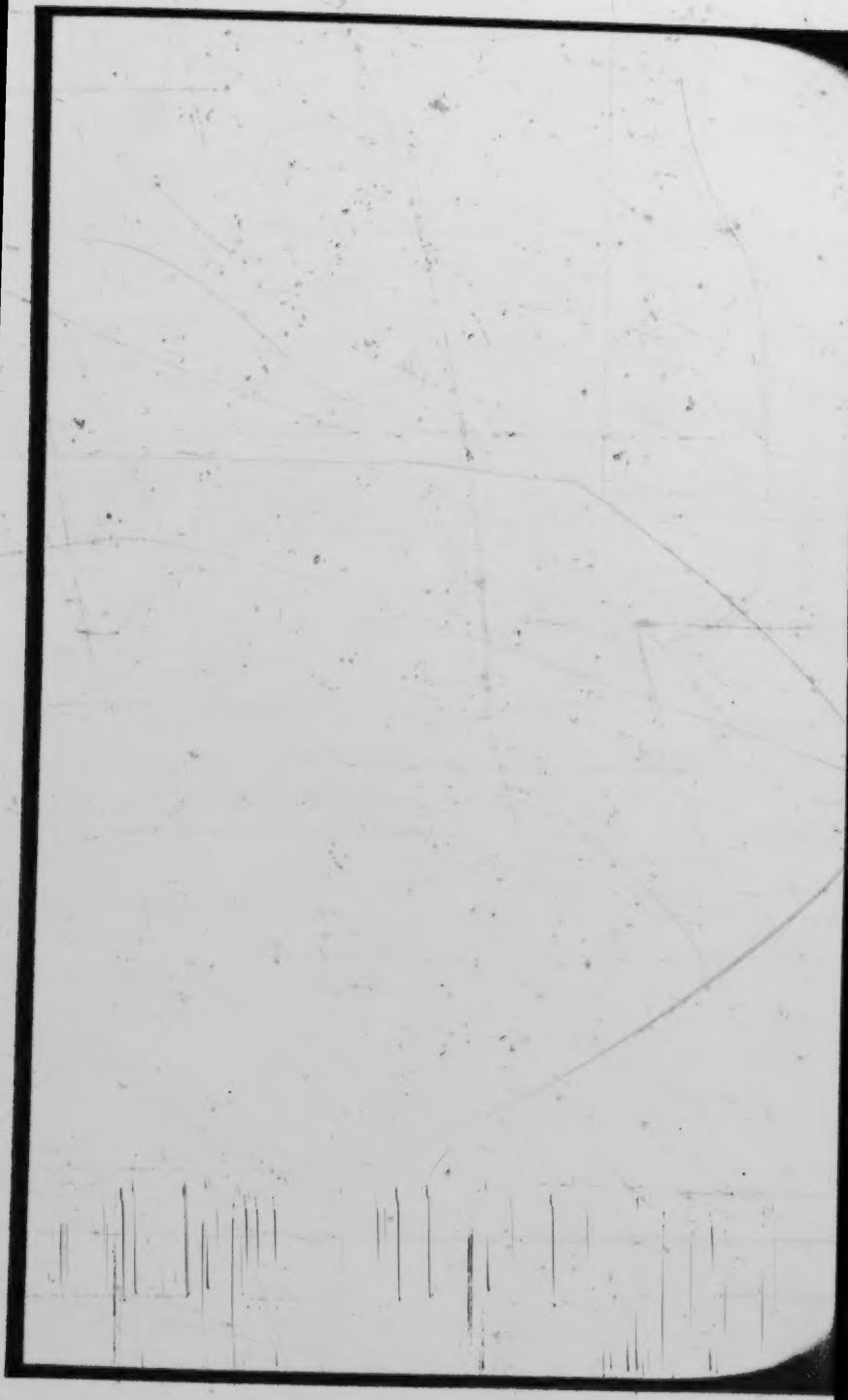

INDEX

BRIEF

PAGE

COUNTER-STATEMENT OF FACTS 1

The Dispute Betewen Ricci And Siegel 2

Proceedings Below 4

SUMMARY OF ARGUMENT 6

ARGUMENT 8

I. THE COMMODITY EXCHANGE ACT PROVIDES COMPREHENSIVE REGULATION OF COMMODITY FUTURES TRADING AND THE PARTICULAR MATTERS BEING CONTESTED 8

A. THE REGULATORY SYSTEM WAS FOUND INPERATIVE TO PROTECT THE NATIONAL PUBLIC INTEREST 8

B. STATUTORY CONDITIONS AND REQUIREMENTS MUST BE MET FOR AN EXCHANGE TO BE DESIGNATED AS A CONTRACT MARKET 9

C. THE COMMODITY EXCHANGE ACT REGULATES WHO CAN ENGAGE IN THE FUTURES TRADING BUSINESS AND THUS RESTRICTS ENTRY 10

D. GENERAL REGULATORY POWERS THE SECRETARY OF AGRICULTURE 10

PAGE

E. MANDATED SELF-REGULATION BY CONTRACT MARKETS SUBJECT TO COMMISSION CONTROL AND JUDICIAL REVIEW OF THE MATTERS CONTESTED SATISFIES PRIMARY JURISDICTION REQUIREMENTS 12

II.. UNRESTRICTED ANTITRUST ATTACKS AGAINST CONTRACT MARKETS WITHOUT PRIOR RESORT TO THE AGENCY WOULD IMPERIL THE CONGESSIONAL POLICY OF SELF-REGULATION 16

III. A COMMON SENSE READING OF THE COMPLAINT MAKES IT OBVIOUS THAT THESE ISSUES SHOULD BE FIRST SUBMITTED TO THE COMMISSION 19

IV. THE COURT OF APPEALS PROPERLY GAVE RECOGNITION TO ACHIEVING THE OBJECTIVES OF THE COMMODITY EXCHANGE ACT WHILE RETAINING JUDICIAL AUTHORITY TO DEAL WITH REMAINING ANTITRUST ISSUES 22

A. PRIMARY JURISDICTION IS A FLEXIBLE CONCEPT 23

B. THE CEA AUTHORIZES RESTRAINTS ON COMPETITION TO FURTHER THE LEGITIMATE PURPOSES OF THE REGULATORY SCHEME AND ITS SELF-REGULATIVE POLICY 25

C. THE CRITERIA ANNOUNCED IN *SILVER* HAVE BEEN PROPERLY APPLIED 27

PAGE

1. The question of primary jurisdiction under the CEA 27
2. The Court of Appeals has properly reconciled antitrust aims with the public policy to be furthered by the CEA 31
3. The Commission's inability to award treble damages and attorneys' fees is no bar to its exercise of primary jurisdiction 33

CONCLUSION 35

SUPPLEMENTAL APPENDIX

RICCI DEPOSITION, JUNE 19, 1969 ..... S.A.1

RICCI DEPOSITION EXHIBIT NO. 10 ..... S.A.3

TRANSCRIPT OF PROCEEDINGS, SEPTEMBER 29, 1969 ..... S.A.4

RULES OF THE CHICAGO MERCANTILE EXCHANGE S.A.5

CITATIONS

CASES:

Board of Trade v. *United States*, 246 U.S. 231 (1918) 21, 26, 27

Civil Aeronautics Board v. *Modern Air Transport, Inc.*, 179 F.2d 622 (2d Cir. 1950) 24

Deaktor v. *Chicago Mercantile Exchange*, (Docket No. 71-1893) 16, 17

Federal Maritime Bd. v. *Isbrandtsen Co.*, 356 U.S. 481 (1958) 34

Minneapolis Grain Exchange v. *Farmers Union Grain Terminal Ass'n*, 75 F. Supp. 577 (D. Minn. 1947) 17, 18

PAGE

Pan American Airways, Inc. v. *United States*, 371 U.S. 296 (1963) 26, 33

Phillips v. *Chicago Mercantile Exchange*, (Docket No. 71-1892) 16, 17

Rice v. *Board of Trade*, 331 U.S. 247 (1947) 9

S.S.W., Inc. v. *Air Transport Ass'n*, 191 F.2d 658 (D.C. Cir. 1951) 34

Securities and Exchange Comm'n v. *Chenery Corp.*, 318 U.S. 80 (1943) 5

Silver v. *New York Stock Exchange*, 373 U.S. 341 (1963) 7, 14, 16, 28, 29, 30, 31, 32

Thill Securities Corporation v. *New York Stock Exchange*, 433 F.2d 264 (7th Cir. 1970) 28

United States v. *Philadelphia National Bank*, 374 U.S. 321 (1963) 33

United States v. *Western Pacific Ry. Co.*, 352 U.S. 59 (1956) 24

STATUTES AND REGULATIONS:

Commodity Exchange Act, as amended,

7 U.S.C. 1, *et seq.* 8

7 U.S.C. 2 11

7 U.S.C. 4 11

7 U.S.C. 5 8

7 U.S.C. 6a 25

7 U.S.C. 6b 25, 26

7 U.S.C. 6c 25

7 U.S.C. 6d 10, 25

7 U.S.C. 6e 10, 25

7 U.S.C. 6f 10, 11, 25

PAGE

7 U.S.C. 6g 10, 25
7 U.S.C. 7 10
7 U.S.C. 7(b) 10, 13, 26, 30
7 U.S.C. 7(d) 26
7 U.S.C. 7a(4) 25
7 U.S.C. 7a(5) 25
7 U.S.C. 7a(8) 12, 29
7 U.S.C. 7a(9) 10, 12
7 U.S.C. 8 30
7 U.S.C. 8(a) 21, 30
7 U.S.C. 9 ..... 11, 26
7 U.S.C. 12 11
7 U.S.C. 12-1 11
7 U.S.C. 12a 29
7 U.S.C. 12a(1) 10, 25
7 U.S.C. 12a(2) 10, 25
7 U.S.C. 12a(3) 10, 25
7 U.S.C. 12a(5) 11
7 U.S.C. 12a(7) 11
7 U.S.C. 13 ..... 12, 26
7 U.S.C. 13(b) 26
7 U.S.C. 13a 13, 30
7 U.S.C. 13b 12, 26
7 U.S.C. 13c(b) 12
7 U.S.C. 15 ..... 11, 26
17 C.F.R. §§ 0.0-0.72 13

PAGE

CONGRESSIONAL:

117 Cong. Rec. 7553 (1971) 28

H.R. Report No. 743, 90th Cong., 1st Sess., to accompany H.R. Bill No. 13094 30

MISCELLANEOUS:

Jaffe, *Primary Jurisdiction*, 77 *Harv. L. Rev.* 1037 (1964) 23, 34

Note, 85 *Harv. L. Rev.* 794 (1972) 23

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COUNTER-STATEMENT OF FACTS

Petitioner has failed to set forth a complete statement of facts material to a consideration of the questions presented.

The Dispute Between Ricci And Siegel

This proceeding involves a dispute between petitioner Ricci and respondent Siegel over the ownership of a membership on the Chicago Mercantile Exchange ("CME"). The facts alleged in the complaint or admitted by Ricci at depositions may be briefly stated.[1]

Siegel hired Ricci as a part-time employee in 1967 and shortly thereafter in May 1967 purchased a CME membership which he registered in Ricci's name. (Ricci Dep. Tr. 5-8; Supp. App. 1-2)[2] On October 24, 1967, Ricci executed and delivered to Siegel an "Authorization to Transfer Membership," on a form prescribed by CME to fulfill the requirements of its Rule 307.[3]

Ricci concedes that the so-called Ricci membership was purchased for $15,000 with Siegel's funds, but claims that Siegel's payment was an advance to Ricci. No documents exist evidencing such a loan. In February 1969, two years after the purchase, a dispute arose between the parties. Ricci claimed ownership of the membership and sought to offset the $15,000 allegedly loaned for the purchase against approximately $18,000 claimed by Ricci against Siegel for floor brokerage fees. (Compl. ¶ 15; App. 11) Significantly, at the time Ricci urged this offset, the price of a CME membership had climbed to $45,000. (Compl. ¶ 18; App. 13)

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[1] Depositions of Ricci were taken prior to presentation of motions to the District Court to dismiss the complaint.

[2] "Supp. App." are references to the Supplemental Appendix attached to this brief.

[3] Rule 307 in pertinent part provided:

"Membership in the Exchange is a personal privilege subject to sale and transfer only as authorized herein. When a member or the legal representative of a deceased or incompetent member desires to sell a membership, he shall sign an authorization to transfer in such form as shall be prescribed by the Board."

On February 11, 1969, Siegel claimed to be the owner of the Ricci membership by reason of the CME "Authorization to Transfer Membership" that had been executed by Ricci. Contemporaneously, Ricci wrote CME directing the revocation of that authorization to transfer. (Compl. ¶¶ 15, 19; App. 11, 13) The President of CME, respondent Harris, replied that "the rules of the Exchange would be observed." (Ricci Dep. Ex. 10; Supp. App. 3)

On February 17, 1969, Ricci and Siegel were invited to and did appear before CME's Board of Governors to air their dispute. (Ricci Dep. Tr. 45; Supp. App. 2) After discussion, the Board of Governors suggested arbitration under CME rules and both parties agreed. But on February 24, 1969, Ricci repudiated his agreement to arbitrate. (Ricci Dep. Tr. 47, 71-73; Ricci Dep. Exs. 2, 3, 6, 7, 8; App. 27-31; Supp. App. 2)[4]

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[4] Ricci's attorney on February 27, 1969, wrote to the Secretary of CME in part as follows:

> "In accordance with rule 500 Mr. Thomas Ricci has been directed by Everette B. Harris to submit the matter of the ownership of his membership to arbitration. It is my interpretation that this matter is not within the scope defined as being arbitrative. To coerce Mr. Ricci to submit is a direct denegation of several of our rules." (Ricci Dep. Ex. 2; App. 30)

Nevertheless, Ricci, in support of his charge that CME had denied him a hearing, has disingenuously contended that CME ignored and circumvented its arbitration rule, stating on page 26 of his brief in the Court of Appeals:

> "The Rules of the Chicago Mercantile Exchange (Rule 5) provide for arbitration of disputes between members, a procedure which, if followed, would have given appellant an opportunity for the full airing of his dispute with Siegel. However, in this case, the Exchange ignored its own rules and circumvented the arbitration requirement by means of a conspiracy between the Exchange officers and Siegel, as charged in the Complaint."

Subsequently, Siegel presented CME with Ricci's "Authorization to Transfer Membership" with the request that the membership be transferred, but CME withheld action until it simultaneously approved the transfer of another membership to Ricci. As petitioner testified:

> "Q. . . . Was there a single day when you were not a member of the Exchange during the period from January, 1969 to April, 1969?
> A. No." (Ricci Dep. Tr. 80; App. 27)

Ricci thereupon filed a treble damage antitrust complaint[5] charging that CME and its officers and Siegel "wilfully, unlawfully, knowingly and maliciously" conspired to prevent Ricci from "continuing as a member of the Chicago Mercantile Exchange" (Compl. ¶ 14; App. 11), "to violate the rules and regulations of the Chicago Mercantile Exchange" (Compl. ¶ 16; App. 12), to cause the transfer of the membership "without a notice or hearing" and thus to deprive him of "his right to act as a member of the Chicago Mercantile Exchange * * * from on or about February 11, 1969, to March 4, 1969." (Compl. ¶ 18; App. 13)

Proceedings Below

Motions to dismiss the complaint for failure to state a cause of action were filed in the District Court. Before the motions were considered, preliminary discovery was pursued, including depositions of Ricci and respondent Melamed, Chairman of the Board of CME. References to these depositions were made in the briefs filed by both parties in support of and in opposition to the motions. CME quoted the admissions in Ricci's depositions that he had received notice and an opportunity to be

[5] The complaint also alleged tortious interference with commercial relationships.

heard on his membership dispute; that arbitration had been suggested, first agreed upon and then rejected by Ricci; and that Ricci was a member of CME at all times.

Ricci had requested the opportunity to take additional depositions of defendants prior to filing his answering brief, but this request was denied, though the District Court was made aware that references to the depositions were being used without objection in presenting the motion to dismiss. (Proceedings of September 29, 1969, Tr. 12-13; Supp. App. 4)

Having concluded to dismiss the complaint, the District Court first requested the submission of findings of fact and conclusions of law (which was done), but then disposed of the matter by an oral opinion. (App. 22)

Before the Court of Appeals, respondents urged that the dismissal motions had been treated as Rule 56 motions for summary judgment since matters outside the pleadings had been submitted without objection and considered by the District Court. The Court of Appeals, however, rejected this contention, holding instead that the District Court only considered the pleadings in ruling on the motions and that the complaint sufficiently alleged a group boycott, a *per se* violation of Section 1 of the Sherman Act.[6] The Court of Appeals then held:

> "[T]hat before a private treble damage action for antitrust violations may be brought against these defendants charging violation of the rules promulgated as a condition to a contract market designation, the

[6] This Court may want to affirm the District Court's ruling as correct even though the basis of the rule was considered incorrect by the Court of Appeals. See *Securities and Exchange Comm'n* v. *Chenery Corp.*, 318 U.S. 80, 88 (1943). Respondents have not cross-appealed or petitioned this Court for review of the Seventh Circuit's decision.

Commodity Exchange Commission and/or the Secretary of Agriculture must have the first opportunity to secure the fulfillment of the statutory duties imposed upon exchanges and their members. The correct remedy in such a case where there is the possibility of a judicial remedy that cannot be granted by the administrative agency is to remand the case to the district court with directions to stay the proceedings until the agency has acted." (App. 45)

SUMMARY OF ARGUMENT

The Commodity Exchange Act provides a comprehensive system of regulation of commodity futures trading on contract markets. Self-regulation by contract markets under the supervision of the Secretary of Agriculture and Commodity Exchange Commission, subject to judicial review, has been established as Congressional policy to achieve the objectives of the Act. Congress has authorized restraints on competition imposed by the agencies and the contract markets to further the legitimate purposes of the regulatory scheme.

Primary jurisdiction is a flexible concept which involves degrees of judicial deference and prior resort to administrative agencies depending upon the regulatory system and the need to promote the proper accommodation between the courts and the agencies.

Prior resort to the Commodity Exchange Commission in this case is appropriate to secure agency consideration of alleged violations of the Commodity Exchange Act and agency implementation of that Act. Upon consideration of the contested matters, the agency may find that a violation occurred for which sanctions under the Commodity Exchange Act should be imposed; that the violation was minor and the public interest does not require the application of sanctions; that no violation occurred;

or that the action of the contract market was taken in good faith to effectuate an imposed statutory duty of self-regulation. In the latter case, justification would exist for the action taken which would excuse the contract market and its officers from an antitrust claim under the rule of reason. Unrestricted antitrust attacks against contract markets without prior resort to the agency would imperil self-regulation.

The criteria expressed in *Silver* v. *New York Stock Exchange*, 373 U.S. 341 (1963), when applied to the Commodity Exchange Act, decisively support the application of the primary jurisdiction doctrine. That Act was expressly amended in 1968, following *Silver*, to grant the Secretary of Agriculture authority to disapprove contract market rules related to the terms and conditions of contracts, trading requirements and minimum financial requirements, and to grant the Commodity Exchange Commission authority to review the enforcement of such rules and, where non-enforcement is found, to impose sanctions, subject to judicial review.

The matters here in controversy involve a garden variety dispute over the rights to a membership. The rule of the Chicago Mercantile Exchange claimed to be violated is a rule relating to trading requirements—since the statute makes it unlawful to trade commodity futures except as a member of a contract market. Accordingly, the enforcement of that rule is directly subject to agency control.

The Court of Appeals properly reconciled antitrust aims with the public policy to be furthered by the Commodity Exchange Act—by submitting the controversy initially to the regulatory agency involved, but retaining jurisdiction in the District Court to consider remaining antitrust aspects and possible remedies which the agency cannot grant.

ARGUMENT

I.

THE COMMODITY EXCHANGE ACT PROVIDES COMPREHENSIVE REGULATION OF COMMODITY FUTURES TRADING AND THE PARTICULAR MATTERS BEING CONTESTED.

A. THE REGULATORY SYSTEM WAS FOUND IMPERATIVE TO PROTECT THE NATIONAL PUBLIC INTEREST.

Congress, in enacting the Commodity Exchange Act ("CEA"),[1] declared that transactions of argricultural commodity futures "are affected with a national public interest" making "regulation imperative" since futures prices are "quoted and disseminated throughout the United States and in foreign countries as a basis for determining the price to the producer and consumer" and that futures transactions are "susceptible to speculation, manipulation, and control [frequently resulting in] sudden and unreasonable fluctuations in the prices thereof * * * which are detrimental to the producer or the consumer and the persons handling commodities." (7 U.S.C. 5)

Congress considered it in the national public interest to provide a free and competitive futures trading market, so that reported futures prices forming the basis for worldwide trade in agricultural commodities and resulting from

[1] Originally enacted as Grain Futures Act in 1922 (42 Stat. 998) and subject to major amendments on June 15, 1936 (49 Stat. 1491) and February 19, 1968 (82 Stat. 30). 7 U.S.C. 1 *et seq.*

bids and offers in established trading pits would competitively reflect the daily appraisal of supply and demand factors by regulated, responsible and informed traders, producers, handlers and consumers.

This Court stressed in *Rice* v. *Board of Trade*, 331 U.S. 247, 250 (1947) (Douglas, J.), that "the Commodity Exchange Act provides comprehensive regulation of trading in futures on commodity exchanges which are designated as 'contract markets' by the Secretary of Agriculture."

B. STATUTORY CONDITIONS AND REQUIREMENTS MUST BE MET FOR AN EXCHANGE TO BE DESIGNATED AS A CONTRACT MARKET.

CME is an Illinois not-for-profit corporation which provides an exchange hall for its members to conduct commodity futures trading by reason of its designation by the Secretary of Agriculture ("Secretary") as a contract market. Only upon the Secretary's designation of the exchange as a contract market and his approval of the particular agricultural commodities sought to be futures traded may such trading legally occur. To be so designated an exchange must comply with specified statutory conditions and requirements, including:

1. Be located at a terminal market where the cash commodity is sold in sufficient volume to reflect general values and where official commodity inspection services are available.
2. Require futures deliveries to be made with commodities conforming to promulgated United States standards from warehouses required to make reports and keep records and subject to government inspection.
3. Enact and enforce rules of government providing that its *members* among other things: a) not disseminate false crop reports or market infor-

mation; b) not manipulate prices or corner any commodity; c) keep records, file reports as directed by the Secretary and be open to government inspection (7 U.S.C. 7(b)); d) comply with provisions of CEA and the Secretary's regulations and orders (7 U.S.C. 7); e) meet minimum financial standards (7 U.S.C. 6f, 7a(9)).

C. THE COMMODITY EXCHANGE ACT REGULATES WHO CAN ENGAGE IN THE FUTURES TRADING BUSINESS AND THUS RESTRICTS ENTRY.

Congress authorized the Secretary to control the persons who may engage in futures trading for others by providing for registration of futures commission merchants and futures floor brokers who must:

1. File applications with the Secretary.
2. Keep books and records open to government inspection and furnish prescribed reports.
3. Meet minimum financial requirements (in this instance established by CME).
4. Segregate customer funds.
(7 U.S.C. 6d, 6e, 6f, 6g, 12a(1)(2)(3))

It is unlawful for a person to solicit, accept or execute a futures contract on a contract market unless so registered. Petitioner Ricci was required to and did register as a futures commission market. In addition he had to be a member of CME before he could engage in the commodity futures business on that exchange.

D. GENERAL REGULATORY POWERS OF THE SECRETARY OF AGRICULTURE.

To accomplish the objectives and purposes of the CEA, the Secretary has been given broad regulatory powers with the right, upon hearings and subject to judicial

review, to impose sanctions on all persons (other than contract markets). He is authorized to:

1. Promulgate regulations "reasonably necessary to effectuate any of the provisions or *accomplish any of the purposes* of this Act." (7 U.S.C. 12a(5); emphasis supplied) Pursuant to this authority, extensive regulations have been promulgated.[8]
2. Conduct investigations. (7 U.S.C. 12, 12-1)
3. Require the maintenance of records and the filing of reports.
4. Disapprove any rule of a contract market which relates "to terms and conditions in contracts" or "other trading requirements" when found to be in violation of CEA or regulations of the Secretary or Commodity Exchange Commision[9] (7 U.S.C. 12a(7)), and to approve rules dealing with minimum financial requirements of exchange members. (7 U.S.C. 6f)
5. Institute hearings upon notice, if he has reason to believe a person (other than a contract market) is manipulating futures prices, has issued false statements or has otherwise violated the CEA or the regulations of the Secretary or Commission. If violations are found, suspension and revocation of trading privileges may be ordered subject to judicial review by a circuit court of appeals. (7 U.S.C. 9, 15)

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[8] 13 F.R. 7834, 14 F.R. 2581, 15 F.R. 4443, 18 F.R. 176, 19 F.R. 6880, 20 F.R. 5288, 6385, 7774, 8043, 21 F.R. 6913, 22 F.R. 6967, 8899, 23 F.R. 6879, 24 F.R. 1288, 26 F.R. 126, 1662, 4887, 27 F.R. 12672, 28 F.R. 5419, 6266, 7471, 30 F.R. 1191, 2258, 6941, 15210, 31 F.R. 4590, 5054, 32 F.R. 7593, 33 F.R. 6088, 8268, 14454, 17900, 34 F.R. 599, 812, 6478, 17511.

[9] The Commodity Exchange Commission ("Commission") consists of the Secretary of Agriculture, Secretary of Commerce and the Attorney General, or their representatives. (7 U.S.C. 2, 4)

6. Issue cease and desist orders, the failure to comply therewith constituting a misdemeanor or felony, punishable by fine and imprisonment. (7 U.S.C. 13, 13b)
7. Report violations of CEA to the Department of Justice for criminal prosecution. Neither the Secretary nor the Commission are required however, "to report minor violations of this Act for prosecution, whenever it appears that the public interest does not require such action." (7 U.S.C. 13c(b))

E. MANDATED SELF-REGULATION BY CONTRACT MARKETS SUBJECT TO COMMISSION CONTROL AND JUDICIAL REVIEW OF THE MATTERS CONTESTED SATISFIES PRIMARY JURISDICTION REQUIREMENTS.

The crux of the commodity futures regulatory system is the Congressional policy that imposes on designated contract markets broad self-regulation responsibilities subject to agency control and judicial review. In order to qualify as a contract market an exchange must adopt and file with the Secretary, subject to his disapproval, statutorily required rules of trading and government. The CEA then requires the contract market to:

> "[E]nforce all • • • rules • • • which relate to terms and conditions in contracts of sale • • • or relate to other trading requirements and which have not been disapproved by the Secretary • • • [and] which provide minimum financial standards and related reporting requirements for futures commission merchants who are members of such contract market and which [rules] have been approved by the Secretary." (7 U.S.C. 7a (8)(9))

Failure of a contract market to enforce such "rules of government" made a condition of its designation, or failure

to comply with any provision of CEA or regulations of the Secretary or Commission, upon hearing by the Commission and subject to judicial review may result in (i) suspension or revocation of its designation as a contract market, or (ii) a cease and desist order, the violation of which may subject the contract market, its officers and agents, to fine and imprisonment. (7 U.S.C. 7b, 13a)

Rules of practice under the CEA have been adopted setting forth the procedures followed by the Secretary in disciplinary proceedings involving any person other than a contract market, and by the Commission governing disciplinary proceedings involving contract markets. (17 C.F.R. §§ 0.0-0.72) These regulations authorize the institution of proceedings before the Commission either on the Commission's own motion or on application of any interested party having information of any CEA violation by a contract market. Hearings are conducted before an appointed referee. Participation in the hearings and proceedings is permitted upon petition for intervention showing good cause. The referee, after the hearings are concluded, is required to file a report with the Commission which forms the basis of argument before, and decision by, the Commission.

In this case, petitioner claims CME violated exchange rules dealing with his right to membership. Since Congress has declared it to be unlawful to trade in specified commodity futures except "where such contract is made by or through a member of a board of trade which has been designated by the Secretary of Agriculture as a 'contract market,'" the rights of membership necessarily involve rules relating to "trading requirements." (Opinion of the Court of Appeals, App. 41) Such rules may be disapproved by the Secretary when filed. These rules must be en-

forced by the contract market when not disapproved, and such enforcement is subject to Commission control.[10]

Mandated self-regulation is the necessary core of the system because of the multitudinous daily transactions involved, the existence of long standing trade customs and the complexities of agricultural marketing. Proper regulation requires comprehensive, yet flexible trading rules, and day-by-day close supervision by exchange officers and committees with market expertise enabling them to make prompt decisions to assure a free and competitive market. In the CEA, as in the Securities Exchange Act, "'the exchanges take the leadership with the Government playing a residual role.'" *Silver* v. *New York Stock Exchange*, 373 U.S. 341, 352 (1963).

Self-regulation is effected in large part by placing the statutory responsibility on contract markets to require their *"members"* to keep records, file reports, meet minimum financial requirements, and comply with the rules of government of the contract market, the statutory provisions and regulations promulgated by the Secretary and the Commission, and to prevent such members from issuing false reports or attempting to manipulate prices or corner the market.

In order to fulfill CME's statutory duties, a detailed and comprehensive set of rules covering its government, trading, membership and other provisions was adopted by

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[10] The Court of Appeals correctly held that "the specific allegations [in the complaint] relate directly to the Commission's and the Secretary's power to designate contract markets and allow the trading in futures by individuals." (App. 43) The United States erroneously expressed doubt as to whether the rules dealing with membership related to "trading requirements" over which the Commission possessed enforcement authority. (U.S. Br. 27-28)

CME and filed with the Secretary. Certain rules were modified or withdrawn to meet objections raised by the Secretary after review. As modified the rules were accepted, and thus became effective rules which had to be enforced by CME. These CME rules include a chapter on "Enforcement of Rules" against members. This chapter provides for notice and hearings before the president of CME and several specially established committees, depending upon the type of offense involved, and authorizes the imposition of sanctions, such as fines, suspension or revocation of trading and membership privileges. Appeal from such determinations may be taken to CME's Board of Governors.[11] The broad purposes of the rules are expressed in Rule 400 as follows:

> "The Board has adopted rules, and from time to time adopts amendments and supplements to such rules, to assure a free and open market on the Exchange, to insure the integrity of contracts on the Exchange, to maintain proper and dignified trading conduct and to provide the maximum protection to the public in its contacts with the Exchange and its members. To that end, the Board has appointed officers and created committees to which it has delegated responsibility for the investigation, hearing and imposition of penalties for violations of the rules of the Exchange." (Supp. App. 5)

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[11] The latest edition of the chapter of CME rules dealing with enforcement is reproduced in the Supplemental Appendix, pages 5-19. Similar enforcement procedures were in effect at the time of the Ricci dispute, including investigations, notice and hearings before the president of CME and hearings and appeals to the Board of Governors.

II.

UNRESTRICTED ANTITRUST ATTACKS AGAINST CONTRACT MARKETS WITHOUT PRIOR RESORT TO THE AGENCY WOULD IMPERIL THE CONGRESSIONAL POLICY OF SELF-REGULATION.

Despite the heavy responsibility of Congressionally imposed self-regulation upon contract markets, every action or decision of the contract market is susceptible to attack as being a concerted action to restrain trade or a group boycott. Such attacks cannot be permitted if the regulatory system is to work. Mr. Justice Stewart, dissenting in *Silver,* pointed to this danger facing a self-regulation system:

> "It may be assumed, I think, that almost every exercise of an exchange's statutory duty of self-regulation would involve an actual or threatened concerted refusal to deal — a 'group boycott.'" (373 U.S. at 367, fn. 1)

The dilemma facing CME in fulfilling its duties of self-regulation is highlighted in two cases now pending in the Seventh Circuit on review of denials of motions for prior resort to the Commission.

In *Phillips* v. *Chicago Mercantile Exchange* (Docket No. 71-1892), a complaint was filed against CME and some of its officers charging a violation of the antitrust laws and the CEA, arising out of an order by CME that certain clearing members liquidate fifty percent of their open interests to insure a free and competitive market. CME issued this order following a determination that the liquidity of March 1970 fresh egg futures contracts was threatened.

In *Deaktor* v. *Chicago Mercantile Exchange* (Docket No. 71-1893), after trading in July 1970 frozen pork belly futures had closed, CME instituted disciplinary proceed-

ings against several members charging them with having violated various rules of the exchange and with having manipulated July 1970 frozen pork belly futures prices. Hearings were conducted for six weeks before the full twelve-man CME Board of Governors, and severe penalties were imposed including revocation of clearing house membership, suspensions from trading for up to three years and substantial fines.[12] Nevertheless, suit was filed by shorts in the market charging that CME had failed to enforce its rules by not acting promptly to prevent manipulations.

Thus, CME is condemned in *Phillips* for taking action during the contract month and in *Deaktor* for not taking action until the contract trading ended. These cases now pending against CME demonstrate the potential danger to contract markets from unrestricted court attacks, if it does, or does not, take action in fulfillment of its self-regulation duties.

Judge Nordbye early recognized the need for primary resort to the agency in view of the operational dilemma facing self-regulating exchanges. *Minneapolis Grain Exchange* v. *Farmers Union Grain Terminal Ass'n*, 75 F. Supp. 577 (D. Minn. 1947). In considering the rule-making powers conferred upon exchanges with respect to membership of cooperatives, the court said:

> "On the one hand, if plaintiff [Minneapolis Grain Exchange] fails to enforce a valid rule, it may be subjected to the penalties provided therefor in the Act. On the other hand, if it enforces an invalid rule,

[12] *The Wall Street Journal* of October 22, 1970, reported: "The governors of the Chicago Mercantile Exchange meted out heavy penalties to four individual members and three member firms for rule violations in trading July 1970 pork belly futures."

it likewise may incur the penalties covering such conduct." (75 F. Supp. at 581)

* * *

"The dilemma which apparently confronts the plaintiff with regard to the applicability of the rules in question to cooperatives must ultimately be determined by the Commission and not by this Court. Suitable machinery is provided in the Act for that very purpose. * * * The intervention of this Court in assuming jurisdiction may give rise to an unfortunate conflict between the rulings of this Court on factual questions and those made by an administrative agency which is expressly clothed by Congress with jurisdiction to determine such a controversy." (75 F. Supp. at 582)

If petitioner's position were accepted and the regulatory system could be avoided by filing a purported antitrust complaint, then every action of a contract market could be subject to judicial attack and the self-regulatory system seriously impeded, if not disrupted. The thrust of the complaint goes to the heart of the regulatory system—the maintenance of a responsible membership organization to achieve compliance with statutorily prescribed and agency approved rules. If the federal court acts here without prior resort to the agency, precedent would be created for repeated imposition of complex and costly antitrust proceedings against contract markets in every situation where action is taken or a decision made by contract markets, even though *bona fide* and within the sphere of their mandated duties.

A delicate balance must be struck to create a climate in which contract markets will be encouraged to bear the burdens and responsibilities of self-regulation, unstifled by the constant threat of harassing antitrust suits, and yet with ultimate responsibility to answer for their derelictions. This balance can be best evolved by the

agency having the express regulatory authority to assure that the designated contract markets are properly enforcing their rules. Only through prior resort to the Secretary and Commission for a consideration of the regulatory issues involved in such attacks can a proper balance be attained, uniform standards evolved and self-regulation made to work. This procedure may result in justification being found for CME's action which, under the rule of reason, would immunize the contract market from antitrust claims. The Court of Appeals quite properly recognized this need to encourage self-regulation by contract markets and strengthen the watch-dog functions of the Secretary and Commission by invoking the doctrine of primary jurisdiction. (App. 43, 44)[13]

III.

A COMMON SENSE READING OF THE COMPLAINT MAKES IT OBVIOUS THAT THESE ISSUES SHOULD BE FIRST SUBMITTED TO THE COMMISSION.

A practical view of the pleadings alone (without considering petitioner's admissions in deposition) establishes that the instant proceeding involves a garden variety dispute over the ownership of a CME membership. No doubt the circumstances regarding the acquisition and ownership of the membership were confused. But this was

[13] Petitioner argues that the alleged group boycott is a *per se* violation which cannot be arguably lawful and therefore resort to the Commission would be a futile procedure. (Pet. Br. 19-23) On this basis, every decision or action of CME in fulfillment of its statutory duties of self-regulation would similarly be a group boycott or other antitrust violation, incapable of justification. Such a position would emasculate the Congressional policy of self-regulation embodied in the CEA.

the very reason CME had to act. The executed authorization to transfer membership by Ricci must have had some meaning. The attempt by Ricci to unilaterally revoke that authorization indicated he had notice of pending CME action on his executed authorization. His belated attempt to set-off an amount allegedly owed him in satisfaction of the original price paid for the membership must be viewed in the light of the threefold increase in the value of the membership from $15,000 to $45,000. In these circumstances, CME was required to decide the matter of trading rights and therefore the issue of ownership.[14]

Under the CEA the issues referred to the Commission for determination in this case would include:

1. What rule, if any, was allegedly violated?
2. Was such a rule properly adopted, filed with the Secretary and not disapproved?
3. What is the trade custom and practice with respect to blank authorizations to transfer memberships and unilateral revocation of such authorizations?
4. What was the purpose of executing the authorization?
5. To what extent, if any, was petitioner denied membership in CME or denied trading privileges?

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[14] It is not claimed that the decision was merely erroneous, but that CME "wilfully, unlawfully, knowingly and maliciously confederated, combined and conspired * * * with Siegel * * * to prevent * * * Ricci from continuing as a member" of CME. (Compl. ¶ 14; App. 11) On the face of the complaint, these antitrust allegations appear frivolous. This may have been the reason for the District Court's dismissal and for the decision of the Court of Appeals to first refer the matter to the Commission to determine whether procedures followed by CME were appropriate to its self-regulation duties and therefore justified under the antitrust laws.

6. Were CME's arbitration procedures, as contained in its filed rules, made available?
7. What action is permissive to CME in resolving membership disputes?

Where there is a dispute as to ownership of or the exercise of the privileges of membership, CME must take action to resolve that dispute. When CME does fulfill this responsibility, and resolves a membership dispute, there is likely to be a losing party. The latter may complain before the Commission that CME failed to enforce its rules or acted contrary to the provisions of the CEA. The issues would be flexibly and expertly resolved by the Commission. The action by CME subject to Commission and then judicial review (7 U.S.C. 8(a)) may be found by the Commission to be justified as in furtherance of the self-regulatory aims of CEA. Thereafter, the District Court may deem CME's action to be within the rule of reason when ruling upon the antitrust claim. *Board of Trade* v. *United States*, 246 U.S. 231 (1918).

The United States in its *amicus* brief (pp. 26-27) points out that no formal proceedings are recorded as having been conducted before the Secretary or the Commission involving membership transfers. Does this not reflect the efficiency of the contract markets in this area of self-regulation? Membership disputes rarely occur and, when they do, are resolved by prescribed arbitration or decision of contract markets, based upon long-standing and accepted trade practices and customs. When so decided, they have not been further questioned.

IV.

THE COURT OF APPEALS PROPERLY GAVE RECOGNITION TO ACHIEVING THE OBJECTIVES OF THE COMMODITY EXCHANGE ACT WHILE RETAINING JUDICIAL AUTHORITY TO DEAL WITH REMAINING ANTITRUST ISSUES.

Petitioner and the United States as *amicus* have mistakenly conceived of the primary jurisdiction concept applied by the Court of Appeals as having "stripped the district court of the power to determine antitrust issues in private actions" (Pet. Br. 10), as creating an "exemption from the antitrust laws" (Pet. Br. 7), and as having found the regulatory system "so pervasive as to exclude or supersede the antitrust powers of the district court." (Pet. Br. 12; U.S. Br. 14)

On the contrary, the Court of Appeals, in view of the charged violation of exchange rules, ordered prior reference to the Commission (the agency with immediate authority to deal with such violations), while retaining jurisdiction in the District Court to consider and determine remaining antitrust issues (including possible justification of the action taken), and to grant appropriate relief. The Court of Appeals specifically held that "the correct remedy in such a case *where there is the possibility of a judicial remedy that cannot be granted by the administrative agency,* is to remand the case to the district court with directions to stay the proceedings until the agency has acted." (App. 45; emphasis supplied)

On the facts alleged, the Commission would determine whether CME's action was (a) contrary to its rules or the regulations of the Secretary or Commission, (b) made in good faith pursuant to the mandated duty of self-regulation, or (c) justifiably necessary to make the self-regulatory

system work. In that connection, the Commission could take into account antitrust principles. (App. 42) It would also have to decide whether a violation of CEA, if found, required imposition of CEA sanctions or was a minor violation which in the public interest should not carry sanctions.

With these agency findings in hand, the antitrust court could then proceed in a more informed manner to determine whether a restraint of trade occurred and, if so, in view of the justification possibly found by the Commission, whether such restraint was permissive under the rule of reason. This application of the primary jurisdiction concept is well within established judicial criteria.

A. PRIMARY JURISDICTION IS A FLEXIBLE CONCEPT.

"Whenever a regulated industry comes under antitrust surveillance, a danger arises that judicial and administrative perceptions of the public interest will conflict." *Note*, 85 *Harv. L. Rev.* 794, 818 (1972). This Court has evolved principles of accommodation with administrative agencies under the concept of primary jurisdiction. But that concept cannot be expressed as a fixed formula since it encompasses varying degrees of judicial deference depending upon the scope, purposes and objectives of the regulatory system. At least five degrees of judicial application of the primary jurisdiction doctrine have been enumerated by commentators, ranging from complete exemption from judicial antitrust control ("exclusive" jurisdiction in the agency) to varying degrees of prior resort to and judicial consideration of agency determinations. *Note*, 85 *Harv. L. Rev.* 794, 821-822 (1972); Jaffe, *Primary Jurisdiction*, 77 *Harv. L. Rev.* 1037, 1038-1039 (1964).

In *Civil Aeronautics Board* v. *Modern Air Transport, Inc.*, 179 F.2d 622, 625 (2d Cir. 1950), Judge Clark stated that "the outstanding feature of the doctrine [primary jurisdiction] is properly said to be its flexibility permitting the courts to make a workable allocation of business between themselves and the agencies."

This Court in *United States* v. *Western Pacific Ry. Co.*, 352 U.S. 59 (1956), speaking through Mr. Justice Harlan, acknowledged this flexibility:

> "The doctrine of primary jurisdiction, like the rule requiring exhaustion of administrative remedies, is concerned with promoting proper relationships between the courts and administrative agencies charged with particular regulatory duties." (352 U.S. at 63)
>
> "No fixed formula exists for applying the doctrine of primary jurisdiction. In every case the question is whether the reasons for the existence of the doctrine are present and whether the purposes it serves will be aided by its application in the particular litigation." (352 U.S. at 64)

Those reasons include:

> "Uniformity and consistency in the regulation of business entrusted to a particular agency are secured, and the limited functions of review by the judiciary are more rationally exercised, by preliminary resort for ascertaining and interpreting the circumstances underlying legal issues to agencies that are better equipped than courts by specialization, by insight gained through experience, and by more flexible procedure." (352 U.S. at 64-65)

B. THE CEA AUTHORIZES RESTRAINTS ON COMPETITION TO FURTHER THE LEGITIMATE PURPOSES OF THE REGULATORY SCHEME AND ITS SELF-REGULATIVE POLICY.

Congress has expressly authorized the agencies themselves, or through self-regulation by contract markets under agency supervision, to place restrictions on competition in furtherance of the regulatory objectives and purposes of the CEA. Such restrictions include:

1. Restrictions on membership and trading privileges imposed by the Secretary (7 U.S.C. 6d, 6e, 6f, 6g, 12a(1)(2)(3)) and contract markets. (CME Rules, Chapter 3—Memberships)

2. Limits on the time, place and date of trading imposed by the Secretary (7 U.S.C. 7a(4)(5)) and contract markets. (CME Rule 705—pit and board trading; Rule 1602—trading months and hours, trading units, price increments for Frozen Pork Bellies. Other commodity contracts have similar provisions.)

3. Statutory prohibitions against specified unfair methods of competition and predatory practices. (7 U.S.C. 6b, 6c)

4. Limits on volume of trading and accumulation of positions by individuals and groups imposed by the Commission (7 U.S.C. 6a) and enforced by contract markets. (*Eg.*, CME Rule 1202 E, F, G—Boneless Beef; Rule 1402 E, F, G—Fresh Eggs; Rule 1602 E, F, G—Frozen Pork Bellies; Rule 1702 E, F, G—Live Cattle)

5. Limits on daily price fluctuations imposed by contract markets. (*E.g.*, CME Rule 1602 D—daily price limits for Frozen Pork Bellies)

Additionally, the CEA has expressly granted antitrust functions to the agencies and provided for the application of antitrust principles. For example:

1. The prevention of monopolization of the market is achieved by authorizing the fixing of maximum limits on the volume of trading and the accumulation of futures positions. (7 U.S.C. 6b) Corners are prevented by rules adopted by contract markets and the imposition of criminal penalties. (7 U.S.C. 7(d), 13(b))

2. Price-fixing is prohibited by rules of contract markets and sanctions imposed by the Secretary which seek to prevent manipulations of prices and sudden and unreasonable price fluctuations. (7 U.S.C. 7(b), 9, 13, 13b, 15)

Congress has thus explicitly authorized these restraints on trade and competition. To the extent that these restraints are imposed as a matter of self-regulation by a contract market rule subject to agency review, it is clear that the agencies "deal with at least some antitrust problems." *Pan American Airways, Inc.* v. *United States,* 371 U.S. 296, 304 (1963).

The United States in its *amicus* brief (p. 23) erroneously seeks to distinguish the Shipping Act, Interstate Commerce Act and Civil Aeronautics Act from the scheme of self-regulation embodied in the CEA by contending that the former three statutes "all evidence a congressional intent either to limit or restrict competition in particular circumstances under agency supervision * * *." We submit that such a Congressional intent is also evidenced in the CEA.

Reasonable restraints by such self-regulating exchanges have been sustained. Thus, in *Board of Trade* v. *United States,* 246 U.S. 231 (1918), this Court justified an exchange rule which prohibited the purchase or sale of cash

grain during the period, from the call (the close of trading) to the opening the next business day, at a price other than the closing bid at the call. Justice Brandeis held:

> "The case was rested upon the bald proposition that a rule or agreement by which men occupying positions of strength in any branch of trade fixed prices at which they would buy or sell during an important part of the business day is an illegal restraint of trade under the Anti-trust Law. But the legality of an agreement or regulation cannot be determined by so simple a test as whether it restrains competition. Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition." (246 U.S. at 238)

Under the circumstances, the exercise of judicial deference through prior submission of the claimed violation of the CEA to the agencies responsible for administration of that regulatory system properly accommodates the respective functions of the agencies and the court.

C. THE CRITERIA ANNOUNCED IN SILVER HAVE BEEN PROPERLY APPLIED.

1. The question of primary jurisdiction under the CEA. The application of the primary jurisdiction concept to a marketing system based upon an expressed Congressional policy of self-regulation, subject to agency and judicial review, involves different criteria than those applied in dealing with regulatory systems such as public utility acts. Chief Judge Swygert, in considering the application of issues of primary jurisdiction to the Securities Exchange Act, found that decisions in other regula-

tory fields "do not provide clear guidance for resolution of this question." *Thill Securities Corporation* v. *New York Stock Exchange,* 433 F.2d 264, 277 (7th Cir. 1970). The Court of Appeals adopted a similar view in this case. (App. 44, fn. 15).

The CEA and the Securities Exchange Act are comparable statutes. The Securities Exchange Act was passed twelve years after the CEA and incorporated many of CEA's features, including the policy of self-regulation by exchanges. In consequence, this Court's standards for application of the primary jurisdiction concept under the Securities Exchange Act are controlling in the CEA field.[15]

While the question of primary jurisdiction was not reached in *Silver* v. *New York Stock Exchange,* 373 U.S. 341 (1963), the criteria announced in that decision properly govern the primary jurisdiction issue raised here. The Court in *Silver* found that the Securities Exchange Act "does not give the Commission jurisdiction to review particular instances of enforcement of exchange rules," and in consequence "obviates any need to consider whether

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[15] Only recently, Senator Jordan (D. South Carolina), Chairman of the Senate Subcommittee on Agricultural Production, Marketing and Stabilization of Prices, stated:

> "[T]he history of regulation and self-regulation in the commodity industry fully justifies the public confidence that it enjoys. The Congress first adopted regulation in the commodity field, and recognized the valuable self-regulatory role of commodity markets, more than a decade before a similar legislative scheme was devised for the securities industry. The Commodity Exchange Act pioneered many protective measures for the public, some of which are only now being applied in other industries." (117 Cong. Rec. 7553 (1971))

petitioners were required to resort to the Commission for relief before coming into court." (373 U.S. at 357-358) The Court made it clear, however, that its decision was limited to the particular facts. The opinion pointed out that:

> "Were there Commission jurisdiction and ensuing judicial review for scrutiny of a particular exchange ruling * * * a different case would arise concerning exemption from the operation of laws designed to prevent anticompetitive activity, an issue we do not decide today." (373 U.S. at 358, fn. 12)

And further:

> "Should review of exchange self-regulation be provided through a vehicle other than the antitrust laws, a different case as to antitrust exemption would be presented." (373 U.S. at 360)

The instant case falls within the category of situations that the *Silver* decision reserved for application of the primary jurisdiction doctrine. In February 1968, following this Court's decision in *Silver* which underlined the absence of SEC authority to review particular instances of enforcement of rules by the exchange, Congress amended the CEA to expressly:

a) Authorize the Secretary to disapprove rules of contract markets relating to terms and conditions of contracts, other trading requirements and minimum financial requirements, which violate any provision of the CEA or regulations of the Secretary or Commission, promulgated to accomplish any of the purposes of the CEA. (7 U.S.C. 12a)

b) Require contract markets to enforce their approved rules. (7 U.S.C. 7a(8))

c) Authorize the Commission, after notice and hearing and subject to judicial appeal, to suspend or revoke the designation of an exchange as a contract market or issue cease and desist orders upon a showing that such exchange has not enforced its rules of government made a condition of designation. (7 U.S.C. 7b, 8, 8(a), 13a)

The CEA, as thus amended, granted authority to the Commission to review contract market enforcement of its rules and thus supplied the deficiency noted in *Silver* to the application of the doctrine of primary jurisdiction.[16]

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[16] In reporting favorably on the 1968 amendments of the CEA, the House Committee included the following statement:

> "The committee feels strongly that full encouragement should be given to cooperative action between the Commodity Exchange Authority and the contract markets. While progress has been made in this direction, the proposed legislation should provide an incentive for still further efforts, encouraged by the background of legal authority.
>
> "Effective regulation of the markets requires the exercise of expert and strictly impartial judgment looking toward reconciling the conflicting forces that are inevitable in commodity futures trading. The committee is impressed by the steps which have been taken in the past toward this end and submits that the enactment of H.R. 13094 will encourage constructive cooperative activity toward minimizing the effects of abusive situations, and thus improve the dignity and usefulness of the futures markets."
>
> (H.R. Report No. 743, 90th Cong., 1st Sess., to accompany H.R. Bill No. 13094, p. 1)

2. The Court of Appeals has properly reconciled antitrust aims with the public policy to be furthered by the CEA.

The central issue facing the Court in these proceedings was stated in *Silver*, with respect to similar self-regulation by securities exchanges, as:

> "[T]he need to reconcile pursuit of the antitrust aim of eliminating restraints on competition with the effective operation of a public policy contemplating that securities exchanges will engage in self-regulation which may well have anti-competitive effects in general and in specific applications." (373 U.S. at 349)

The question posited in *Silver* was whether there was "justification derived from the policy of another statute" to excuse an exchange action under the rule of reason from a claimed antitrust violation. (373 U.S. at 348-349) As the majority put it:

> "The entire public policy of self-regulation, beginning with the idea that the Exchange may set up barriers to membership, contemplates that the Exchange will engage in restraints of trade which might well be unreasonable absent sanction by the Securities Exchange Act. * * * But, under the aegis of the rule of reason, traditional antitrust concepts are flexible enough to permit the Exchange sufficient breathing space within which to carry out the mandate of the Securities Exchange Act. * * * Although, as we have seen, the statutory scheme of that Act is not sufficiently pervasive to create a total exemption from the antitrust laws, * * * it is also true that particular instances of exchange self-regulation which fall within the scope and purposes of the Securities Exchange Act may be regarded as justified in answer to the assertion of an antitrust claim." (373 U.S. at 360-361)

This policy of self-regulation and the stated criteria for accommodation of the two systems are precisely applicable to the CEA. Mr. Justice Stewart, in his dissent in *Silver*, cogently expressed the principles that should control the application of antitrust claims to self-regulating exchanges under the Securities Exchange Act (and we submit that the same principles apply to exchanges under the CEA), as follows:

> "The purpose of the self-regulation provisions of the Securities Exchange Act was to delegate governmental power to working institutions which would undertake, at their own initiative, to enforce compliance with ethical as well as legal standards in a complex and changing industry. This self-initiating process of regulation can work effectively only if the process itself is allowed to operate free from a constant threat of antitrust penalties. To achieve this end, I believe it must be held that the Securities Exchange Act removes antitrust liability for any action taken in good faith to effectuate an exchange's statutory duty of self-regulation. The inquiry in each case should be whether the conduct complained of was for this purpose. If it was, that should be the end of the matter so far as the antitrust laws are concerned—unless, of course, some antitrust violation other than the mere concerted action of an exchange and its members is alleged." (373 U.S. at 371)

Under these principles, it was appropriate for the Court of Appeals to require prior resort to the Commission to determine whether a CME rule was violated; whether CME acted in good faith to effectuate its statutory duty of self-regulation; whether disciplinary action under the CEA should be imposed; or whether CME's action involved a minor violation which in the public interest did

not require disciplinary measures to be taken. The Commission's decision is subject to judicial review. When filed with the District Court, the agency's determination may be considered in connection with the antitrust claim.

By this means, the integrity of the self-regulation system is protected in the specific areas of the Commission's authority. *United States* v. *Philadelphia National Bank*, 374 U.S. 321 (1963), so heavily relied upon by petitioner and the United States as *amicus*, fully supports this view. The Court there said with respect to primary jurisdiction:

> "That doctrine requires judicial abstention in cases where protection of the integrity of a regulatory scheme dictates preliminary resort to the agency which administers the scheme. • • • Court jurisdiction is not thereby ousted, but only postponed." (374 U.S. at 353)

3. The Commission's inability to award treble damages and attorneys' fees is no bar to its exercise of primary jurisdiction.

Petitioner argues further that any judicial deference to the Commission would be futile and therefore improper since neither the Secretary nor the Commission can grant the relief sought, namely treble damages and an allowance of attorneys' fees. (Pet. Br. 23-26) The United States as *amicus* seems also to so argue. (U.S. Br. 20 fn. 9, 24) This Court answered that contention in *Pan American Airways, Inc.* v. *United States*, 371 U.S. 296, 313 fn. 19 (1963), as follows:

> "If it were clear that there was a remedy in this civil antitrust suit that was not available in a § 411 proceeding before the C.A.B., we would have the kind of problem presented in Hewitt-Robins Inc. v. Eastern Freight-Ways, Inc. 374 U.S. 84, • • • where liti-

gation is held by a court until the basic facts and findings are first determined by the administrative agency, so that the judicial remedy, not available in the other proceeding, can be granted."

See also, Jaffe, *Primary Jurisdiction*, 77 *Harv. L. Rev.* at 1057; *S.S.W., Inc.* v. *Air Transport Ass'n*, 191 F.2d 658 (D.C. Cir. 1951).[17]

[17] Even where an agency does not have the power to immunize from antitrust liability, prior recourse has been directed on "practical considerations [which] dictate a division of functions • • • under which [the agency] makes a preliminary, comprehensive investigation of all the facts, analyzes them, and applies to them the statutory scheme as it is construed." *Federal Maritime Bd.* v. *Isbrandtsen Co.*, 356 U.S. 481, 498 (1958).

CONCLUSION

The judgment of the Court of Appeals should be affirmed.

Respectfully submitted,

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July 1972

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1971

No. 71-858

THOMAS RICCI,

Petitioner,

vs.

CHICAGO MERCANTILE EXCHANGE, an Illinois not-for-profit corporation, EVERETTE B. HARRIS, WILLIAM PHELAN, LEO MELAMED, THE SIEGEL TRADING COMPANY, a corporation, and JOSEPH E. SIEGEL,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

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SUPPLEMENTAL APPENDIX

EXCERPTS FROM ORAL DEPOSITION OF THOMAS RICCI TAKEN ON JUNE 19, 1969, IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, DOCKET NO. 69 C 1030

Examination By Mr. Freeman For The Defendants

Q. When did you come with Siegel?

A. I think it was in 1967.

Q. Was this the first job you had that involved the Chicago Mercantile Exchange?

A. Yes, it was.

Q. Now, what was your function at Seigel?

A. When I first came to work for Seigel I

started out as a runner on the floor. My function
7 was to bring orders to the brokers in the pit.

From there, I became a phoneman on the floor. My function was to write up orders and give them to the runners.

Then, I was moved up into the office. I ran the order desk upstairs. My function there was to take orders from different offices and put them into the different commodity exchanges.

8 Q. When did you start working for Siegel?

A. I think it was 1967.

Q. When did you become a member of the Chicago Mercantile Exchange? • • • Was it May of 1967?

• • •

The Witness: Yes.

45 Q. Now, Mr. Ricci, did you have occasion to appear before the Board in connection with the attempt by Mr. Joe Siegel to transfer your membership in February, 1969?

A. Yes, before the attempt was made, I had.

• • •

Q. And at that time you made a statement before the Board, didn't you?

A. I may have. I said a lot of things. The only thing I said would be a statement, correct.

Q. Did you admit that you had signed the authorization to transfer on October 24, 1967 when it was presented?

A. Yes, I did.

47 Q. Was there ever a suggestion at that time made that the controversy be submitted to arbitration as the easiest method of resolving it?

A. For the membership?

Q. The membership question, yes, as to whether or not it belonged to Joe Siegel or Tom Ricci?

A. Yes.

Q. Did you before the Board agree that you would go to arbitration?

A. Yes.

RICCI DEPOSITION EXHIBIT NO. 10

February 13, 1969

Mr. Harry Fortes
110 N. Franklin Street
Chicago, Illinois

Dear Mr. Fortes:

This is in response to your letter of February 11, relative to your client, Exchange member Mr. Thomas C. Ricci. To date I have received no authorization to transfer this membership, and, of course, it has not been transferred.

Be assured that the rules of the Exchange will be observed in this or any related matter which may come up in the future.

Sincerely yours,
Everette B. Harris
President

TRANSCRIPT OF PROCEEDINGS BEFORE THE HONORABLE JAMES B. PARSONS, ONE OF THE JUDGES OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS IN CHICAGO, ILLINOIS, HELD ON SEPTEMBER 29, 1969, AT 10:15 A.M.

Present:

Mr. Fred J. Ginsberg,
on behalf of the Plaintiff;

Mr. Jerrold E. Salzman,
on behalf of Defendant Chicago Mercantile Exchange;

Mr. Max Chill,
on behalf of certain defendants.

The Court: When you have a motion to dismiss, I would rather you go ahead with that, brief it, if you have to, and let me decide that before you expend the time and energy of going ahead with depositions. If you need to depose your parties in order to oppose a motion to dismiss that is made on its face, unless that motion to dismiss is supported by affidavits—

Mr. Ginsberg: I think their motion to dismiss quotes from the deposition taken of the plaintiff.

Mr. Salzman: Of the plaintiffs.

Mr. Ginsberg: Absolutely. That is exactly the point. We say that we have to take the depositions of the defendants, to attach that to our reply to counteract some of the statements that they have got in their motions.

The Court: Do you mean the plaintiff didn't tell the truth?

Mr. Ginsberg: Oh, he sure told the truth.

Mr. Salzman: That is our point, your Honor. They are taking our people to counteract their own persons' statements, and that doesn't seem to follow, does it?

November, 1971

RULES OF THE CHICAGO MERCANTILE EXCHANGE

CHAPTER 4 — ENFORCEMENT OF RULES

400. GENERAL PROVISIONS.—The Board has adopted rules, and from time to time adopts amendments and supplements to such rules, to assure a free and open market on the Exchange, to insure the integrity of contracts on the Exchange, to maintain proper and dignified trading conduct and to provide the maximum protection to the public in its contacts with the Exchange and its members. To that end, the Board has appointed officers and created committees to which it has delegated responsibility for the investigation, hearing and imposition of penalties for violations of the rules of the Exchange. The delegation of such responsibility and authority shall in nowise limit the authority of the Board to deal ultimately with all rule violations, either on its own initiative or upon appeal, and nothing in this chapter shall release the president of his duties and responsibilities to secure enforcement of the rules of the Exchange.

401. CLASSIFICATION OF OFFENSES.—Offenses against the Exchange shall be major offenses and minor offenses. Major offenses shall be punishable by expulsion, suspension, fine of not more than $10,000.00, or by both suspension and fine. Minor offenses shall be punishable by a fine of not more than $2,500.00 or suspension for not more than one year, or both.

402. MAJOR OFFENSES.—It shall be a major offense:

a. to be interested in, operate, or knowingly represent or make any transaction with a bucket-shop;
b. to be guilty of any dishonest conduct;
c. to be guilty of fraud or any act of bad faith;
d. to make or report a false or fictitious trade;
e. to attempt extortion;
f. to buy or sell any commodity intending to make default on such purchase or sale;

g. to act as both buyer and seller in the same transaction;

h. to manipulate or attempt to manipulate prices or to corner or attempt to corner the market;

[1] i. to make a material misstatement to the Board, or to a Committee, or any information supplied to the Exchange or its Officers;

j. to knowingly disseminate false, misleading or inaccurate reports concerning crop or market information or conditions that affect or tend to affect the price of any commodity upon the Exchange;

k. to be found guilty of a second violation of the same rule or the same minor offense;

l. to trade or accept margins after insolvency;

m. to refuse to appear before the Board, president, Business Conduct Committee, Clearing House Committee or Floor Practices Committee at a duly convened investigative hearing or in connection with any investigation; to refuse to fully answer all questions and produce all books and records at such hearing or investigation or to testify falsely;

n. to make use of or reveal any confidential information obtained by reason of participating in any investigative proceedings or any hearing;

o. to accept directly or indirectly a trade for the account of a non-member employed on the floor of the Exchange;

p. for a member, clearing member, or sub-broker to permit the use of its facilities by members or non-members in a manner that impairs the dignity or degrades the good name of the Exchange, or creates a market or other situation detrimental to the Exchange, or results in violation of the speculative limit rules, or effectuates manipulations or corners, or attempts of either;

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[1] Revised August, 1971.

q. for a clearing member or sub-broker to fail to maintain minimum financial requirements;
r. to commit an act which is substantially detrimental to the interest or welfare of the Exchange;
s. to refuse to submit to arbitration any dispute which the president or the Board, on appeal, decides should be arbitrated; or to refuse to comply with a final arbitration award;
t. to refuse, after hearing, to comply with an order of the Board, the president or any hearing committee; or
u. to violate a rule which recites such violation is a major offense.

403. MINOR OFFENSES.—It shall be a minor offense:
a. to be guilty of dishonorable conduct;
b. to be guilty of uncommercial conduct;
c. to be guilty of any conduct which has a manifest tendency to impair the dignity or the good name of the Exchange;
d. to interpose a Statute of Frauds defense to any claim for breach of an Exchange contract;
e. to make a false entry upon a clearing sheet;
f. to violate any rule, the violation of which is not a major offense.
[1] g. To circulate or aid in the circulation in any manner of rumors which tend to reflect on the integrity of any contract.

404. DELEGATION AND JURISDICTION OF ENFORCEMENT AUTHORITY.

A. The President

1. Rule Violations—

It shall be the duty of the president to enforce the rules of the Exchange, and to this end: he shall have available to him at all times the facilities of the Department of Audits and Investigations to conduct

[1] Adopted August, 1971.

investigations of rule violations and market conditions; he shall have authority to inspect the books and records of all members; he may require any member to appear before him and produce his books and records and answer questions regarding a violation of the rules of the Exchange.

If the president suspects that a rule of the Exchange has been violated, he shall make an investigation or cause the Department of Audits and Investigations to conduct an investigation. If the president has reasonable cause to believe that any member has violated an Exchange rule, the president shall notify such member in writing of the violation of which he is suspected and shall fix a time and place for a hearing, at which time the member shall appear and have the right to be heard in his own behalf. Dependent upon the violation involved, such hearing shall be held at the president's direction either before: the president; Business Conduct Committee; Clearing House Committee; Floor Practices Committee; or the Board.

[1] 2. Emergencies—

If the president determines:

a. that the free and orderly market in a commodity is or is likely to be disrupted; or

b. that the ordinary or normal functioning of the Exchange has been or is likely to be disrupted,

he may, with the consent of the chairman of the board and either the chairman of the Business Conduct Committee or the Clearing House Committee take such action or direct any member, clearing member, sub-broker, or member by virtue of assignment of rates, to take such action that may, in the president's sole discretion, seem necessary to prevent, correct or alleviate such condition.

3. Emergency Financial Conditions—

If the president determines that the financial condition of any clearing member or sub broker is such

[1] Revised October, 1971.

as his continued operation would jeopardize the integrity of the Exchange, the president may proceed against said clearing member or sub-broker in accordance with rule 907, 929 or 930.

The Board may exercise any of the authority and power which by these rules are vested in the president, any committee or other representatives of the Exchange. The Board may also, when it deems that an emergency exists, stop trading in any future contracts and, notwithstanding any other Exchange rules, determine the manner in which deliveries shall be made or fix a settlement price at which all such contracts shall be closed out.

All Exchange contracts shall be subject to this rule and are accordingly modified to the extent necessary to comply with the action taken hereunder.

B. The Business Conduct Committee

The Business Conduct Committee shall have general supervision of matters described in Rule 222, and shall have the jurisdiction to enforce the rules pertaining to the following:

1. Attempts to manipulate and manipulations of prices and attempts to corner and corners of any commodity on the Exchange;
2. Conduct of member detrimental to the good name of the Exchange; and
3. Business conduct of and compliance with Exchange rules and regulations by members, including conduct affecting non-members and the public, except insofar as jurisdiction over the conduct of clearing members, sub-brokers and solicitors is assigned to the Clearing House Committee by 404C hereof.

The Business Conduct Committee may conduct hearings on rule violations falling in the above defined categories either on its own initiative, by reference from the president, the Audits and In-

vestigations Department, the Public Relations Department, the Floor Practices Committee or any other committee.

C. The Clearing House Committee

The Clearing House Committee shall have general supervision of matters described in Rule 223 and shall have jurisdiction to enforce the rules pertaining to the following:

1. Manner of clearing trades;
2. Functioning of the Clearing House;
3. The financial integrity of clearing members and sub-brokers; and
4. Business conduct of and compliance with Exchange rules and regulations by clearing members, sub-brokers and solicitors, except insofar as jurisdiction over manipulations and corners is assigned to the Business Conduct Committee by 404B hereof.

The Clearing House Committee may conduct hearings on rule violations falling in the above defined categories either on its own initiative or by reference from the president or the Audits and Investigations Department.

D. The Floor Practices Committee

The Floor Practices Committee shall have general supervision of matters described in Rule 226 and shall have general jurisdiction to enforce the rules contained in Chapter 7 and all rules relating to floor practices and trading ethics. The Floor Practices Committee may conduct hearings on rule violations falling in the above defined categories either on its own initiative or by reference from the president.

405. INITIAL INVESTIGATION BY PRESIDENT AND ASSIGNMENT FOR HEARING.—If after investigation the president has reasonable cause

to believe that a member has violated a rule of the Exchange and that the matter may best be dealt with by the president, he shall set the matter for hearing by his own office. If the president has reasonable cause to believe an offense has occurred which may best be dealt with by the Business Conduct Committee, Clearing House Committee or Floor Practices Committee, he shall transmit to the chairman of the committee having jurisdiction of the offense a written statement setting forth the charges against the member involved and request that a hearing be held. If after investigation by the president, or after hearing before the Business Conduct Committee, Clearing House Committee or Floor Practices Committee there is reasonable cause to believe that the violation of the rule or offense committed is of sufficient importance to warrant a direct hearing before the Board, then the president or committee chairman shall file with the chairman of the board his written statement setting forth the charges or, if a hearing has been held, the findings and recommendations of the hearing body.

406. CONDUCT OF HEARINGS.—All hearings shall be commenced by notifying the member under investigation in writing of the offense with which he is charged. A reasonable time and place for the hearing shall be included in the notice. The hearing body shall have power to compel any member to attend, to testify and to produce all books and records relevant to the subject matter under investigation.

The members of the hearing body may actively question and examine all evidence or they may request an official of the Department of Audits and Investigations to conduct the examination. The member under investigation may testify and produce evidence in his own behalf and cross-examine any witness.

The member may be represented by another member of the Exchange, but may not be represented by legal counsel or by a member of the Board or of the investigating committee.

All testimony and documents produced in connection with a hearing conducted pursuant to this Chapter 4 shall be deemed confidential and shall not be revealed or otherwise used, except in connection with disciplinary proceedings resulting from that hearing. After hearing, the hearing body shall determine guilt or innocence. A member found not guilty shall not again be charged with or tried for the same offense. In all cases, the chairman of the hearing committee shall promptly file a written report of its findings, decisions or recommendations with the president, the chairman of the board, the full committee (if the hearing committee is a subcommittee thereof) and the member who was charged.

407. HEARINGS, FINDINGS AND PENALTIES.[1]

A. Original Hearings before the Board

Whenever an original hearing is scheduled to be held before the Board, the Chairman shall determine whether the matter shall be held before the Board as a whole, or before a Hearing Committee of the Board.

1. Board as a Whole—In the event the matter is held before the Board as a whole, it shall be held before at least a quorum of the Governors at a duly constituted meeting. The hearing shall be conducted by the Chairman and shall require the affirmative vote of seven Governors for a finding of guilty on a major offense and the affirmative vote of a simple majority for a finding of guilty on a minor offense.
2. Hearing Committee—In the event the matter is held before a Hearing Committee of the Board,

[1] Revised August, 1971.

the Chairman shall appoint four Governors to serve on said Committee. The hearing shall be conducted by the Chairman, or in his absence or upon his order, by the First Vice-Chairman or Second Vice-Chairman. A unanimous decision by the members of the Hearing Committee shall be considered the action of the Board as a whole.
In the event a unanimous decision by the Hearing Committee cannot be obtained, the Chairman shall refer the matter to the Board as a whole. The Board shall review the evidence submitted to the Hearing Committee at a special or regular meeting and shall vote on the matter in accordance with Rule 407 A-1 hereof.

B. Hearings before the President

Hearings before the president shall be conducted by the president, or in his absence by the vice president in charge of audits and investigations. In the event that the president determines that member is guilty of the violation or offense charged, he may order suspension for a period not to exceed one year or assess a fine within the limits of Rule 401, or both. In case of a finding of guilt, the president shall promptly provide the member with the written findings and the amount of any fine or term of suspension. The member shall pay any fine assessed within five days of receipt of notice, or be denied all privileges of membership thereafter until such fine is paid.
If the president decides that the matter is of major importance, he may refer the matter to the Board for hearing.

C. Hearings before the Business Conduct Committee

1. Rule Violations—
Hearings by the Business Conduct Committee shall be before the members or alternates of that committee and shall be conducted by the committee chairman, who shall not have a vote.

The committee shall decide by a majority vote whether the member is guilty of the violation or offense charged. If the accused member is found guilty, the Business Conduct Committee may:

a. Order the member to cease and desist from the conduct found to be in violation of the rules or contrary to the best interest of the Exchange.
b. Order the member to liquidate such portion of the open contracts in the member's proprietary or customers' accounts, or both, as the committee deems necessary to insure the integrity of the Exchange contracts or to insure an orderly and liquid market.
c. Order the member to deposit such additional margins with the Exchange as the committee deems necessary to protect the integrity of open contracts.
d. Impose a period of suspension against the member not to exceed 10 days.
e. Impose a fine against the member not to exceed $5,000.00.
f. Impose advertising restrictions pursuant to these rules.

If the committee shall decide by a majority vote that the matter is of major importance or might warrant a penalty in excess of its own authority, the chairman of the committe shall refer the matter to the Board for further hearings and decision.

2. Emergency Actions—

Whenever, as a result of investigation by the Department of Audits and Investigations, the Business Conduct Committee determines that the integrity of any contract is in jeopardy, or the liquidity of any contract is threatened, it may:

a. Order the liquidation of such portion of the open contracts in any member's proprietary or customers' accounts, or both, as the committee deems necessary.

b. Order a member or his customers to deposit such additional margin with the Exchange as the committee deems necessary.

In addition to the foregoing, the committee may, with consent of both the president and the chairman of the board:

c. Order that trading in a specific contract be limited to closing of open positions.

d. Order that trading be limited to a confined price range.

e. Order such other action as is deemed necessary to insure the integrity of the Exchange contracts or to insure an orderly and liquid market.

D. Hearings before the Clearing House Committee

Hearings by the Clearing House Committee shall be conducted by the chairman of the committee, who shall not have a vote, and three members of the committee chosen by lot from among those available committee members who have not previously participated in a hearing, or from among the available committee members who have had the least participation.

The hearing sub-committee shall decide by a majority vote whether the member is guilty of the of the violation or offense charged and its decision shall be considered the action of the full Clearing House Committee.

If the accused member, after hearing, is found guilty or is found to be in a financial condition which jeopardizes the integrity of the Exchange, the hearing sub-committee may:

1. Order the member to cease and desist from the conduct found to be in violation of the rules or contrary to the best interests of the Exchange.
2. Order the member to deposit such additional margin with the Exchange as is deemed necessary to protect the integrity of open contracts.
3. Prescribe such additional capital requirements as it deems necessary.
4. Prescribe such position limitations as it deems necessary.

5. Impose a fine against the member not to exceed $5,000.00.
6. Suspend a clearing member or sub-broker if it finds that the financial condition of such clearing member or sub-broker is such that it jeopardizes the integrity of the Exchange, subject to approval of any two of the following: the president, the chairman of the board, and chairman of the Clearing House Committee. In the event of a suspension, the member's facilities and open trades shall remain suspended for liquidation only, until the matter is finally determined by the Board.

If the sub-committee, by majority vote, shall decide that the matter is of major importance or might warrant a penalty in excess of its own authority, the chairman of the sub-committe shall refer the matter to the Board for further hearings and decision.

E. Hearings before the Floor Practices Committee

Hearings by the Floor Practices Committee shall be conducted by the chairman of that committee, who shall not have a vote, and shall be held before the members of that committee.

The committee shall decide by a majority vote whether the member is guilty of the violation or offense charged. If the accused member is found guilty, the Floor Practices Committee may:

1. Order the member to cease and desist from the conduct found to be in violation of the rules or contrary to the best interests of the Exchange.
2. Impose a period of probation.
3. Impose a fine against the member not to exceed $1,000.00.

If the committee, by majority vote, shall decide that the matter is of major importance or might warrant a penalty in excess of its own authority, the chairman of the committee shall refer the matter for hearing and decision to the Board, or to the Business Conduct Committee.

408. APPEAL TO THE BOARD.—If, after hearing, a member is found guilty of an offense, he may appeal to the Board within 10 days after the receipt of the findings and decision of the president, Business Conduct Committee, Clearing House Committee or Floor Practices Committee, as the case may be. On such appeal, the Board shall review the charges levied, the record made before the president or committee, the findings and decision appealed from, the notice of appeal and any written memorandum which the accused member may wish to file, provided such memorandum is filed with the secretary of the Exchange within five days after notice of appeal.

[1] Appellate hearings before the Board shall be conducted by the chairman and require the presence of at least nine other governors. An affirmative vote of two-thirds shall be necessary to set aside or modify the findings and decision of the president or the committee from which the appeal was taken.

Filing of notice of appeal shall not suspend the order or decision of the president or committee unless the president or the chairman of the involved committee specifically directs that the decision be stayed.

409. REHEARING.—A member may have a rehearing by the Board if a petition is filed within 10 days of initial action by the Board and it is established that the disciplinary action taken was the result of false testimony, was too severe or otherwise improper.

410. EFFECT OF SUSPENSION.—A suspended member may not trade on the Exchange in person or by employee or by broker, except at the regular commission rates of a non-member, or have any of the privileges of a member during the time of his suspension. Members are forbidden to trade as broker or employee for a suspended member except at the regular non-member's commission rate. A suspended member may be reinstated upon such conditions as

[1] Revised October, 1971.

the Board may impose. A suspended member shall not be allowed to visit the Exchange floor during trading hours except in the instance where special permission is granted by the Board and such permission does not conflict with C.E.A. findings.

411. EXPELLED MEMBER.—An expelled member shall forfeit all privileges of membership, and may not trade on the Exchange, either in person or by employee, or by broker, except at the regular commission rate of a non-member. An expelled member shall not be allowed to visit the Exchange floor during trading hours.

The membership of an expelled member must be sold and transferred on the books of the Exchange within 30 days after the member's expulsion. If, after 30 days, the membership has not been so transferred, it shall be sold at public auction under the direction of the president, following the procedures set forth in Rule 307.

412. OPEN TRADES OF SUSPENDED OR EXPELLED CLEARING MEMBERS.—When a clearing member is suspended or expelled for a violation of these rules, other than for insolvency or default on his obligation to the Clearing House, he may designate a floor broker to close out his open trades in accordance with the Board's direction.

413. PUBLICATION OF RULE VIOLATIONS.—Whenever a member is found guilty of a major offense, or a minor offense which in the opinion of the president is of major consequence, his name together with the rule violated and the penalty assessed, shall be included in the monthly Executive Reports to the membership.

414. SUSPENSION OR EXPULSION VACATES OFFICE.—Any officer, governor or member of any committee of the Exchange, when suspended or expelled from membership, shall be considered automatically removed from office or position.

415. REINSTATEMENT BAR TO FURTHER DISCIPLINE.—If a member is reinstated after suspension, or re-elected after expulsion, he shall not again be disciplined for the original offense.

416. MEMBER'S INDEMNIFICATION LIABILITY TO THE EXCHANGE.[1]—Each member, clearing member, sub-broker, associate-broker or member by virtue of assignment of rates, shall indemnify and hold the Exchange harmless for the full amount of any judgments or settlements, paid by it in respect to any legal proceeding brought against the Exchange as a result of an alleged violation of any laws or rules of the Exchange by said member, clearing member, sub-broker, associate-broker, or member by virtue of assignment of rates, or as a result of an alleged failure of the Exchange to detect, prevent, or otherwise act against said alleged violation.
Any charges arising out of this rule shall be subject to liens as provided in Rule 309, paragraph (a).

(End of Chapter 4)

[1] Adopted August, 1971.